

Labor market slowdown is not expected to emulate the 90s

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Structural changes in the economy should lower the impact on the labor market

The recovery of economic growth in Brazil over the last few years has been an important factor for explaining the drop in the Brazilian unemployment rate. Between 2003 and 2008, this rate shrank from 12.3% to only 7.9%. Such a strong drop, of 4.4 percentage points, was significant both in absolute terms and when compared to other countries (see Brazilian Economic Insights Nº 61.).

Nonetheless, the macroeconomic scenario underwent a substantial deterioration over the last few months in light of the downturn of the world economy. The financial crisis has strongly affected the global scale of

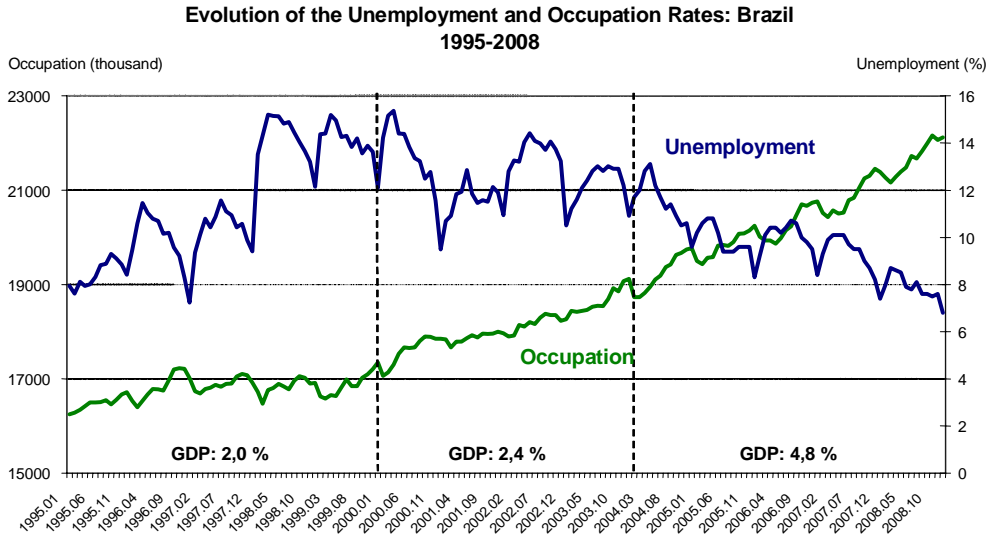
activity and employment. The leading developed economies are already facing recession. In the case of the US, the unemployment rate has been increasing significantly since the second half of 2007.

In Brazil, the crisis has already begun to negatively impact the labor market. The generation of registered work, which has managed an expressive recovery over the last few years, was especially affected during 4Q2008. Net creation of employment (the number of hirings excluding dismissals) was markedly negative in December.

The purpose of this report is to address the trends for the evolution of the

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Graph 1



Source: PME/IBGE (old and new groups – linearly interpolated)

Brazilian labor market in the near future. Specifically, an issue to be covered is whether lower growth in view of the world crisis would possibly yield a substantial rise in the unemployment rate, as observed in the second half of the 90s.

The main focus lies in the fact that the Brazilian economy has undergone significant structural changes over the last ten years, which has been helping to preserve employment. Thus, a sharp upsurge in the unemployment rate, such as that observed in late 90s, should not be expected.

The recent evolution of the Brazilian labor market

The behavior of the Brazilian labor market will be reviewed with a focus on two variables: the level of occupation (generation of employment) and the unemployment rate¹. Graph 1 shows the evolution of these variables as of 1995 (the period after adopting the Brazilian Real as the country's official currency), and the timeline is subdivided as follows: 1995-1999; 2000-2003 and 2004-2008. Data are collected from the Monthly Employment Survey of the Brazilian Institute of Geography and Statistics (*Pesquisa Mensal de Emprego/Instituto Brasileiro de Geografia e Estatística*) PME/IBGE,

¹ People are considered to be unemployed when they are not currently employed, are available to work and have adopted active measures to finding a job over a certain period of reference.

which covers the metropolitan areas of cities, such as Recife, Salvador, Belo Horizonte, Rio de Janeiro, São Paulo and Porto Alegre².

Between 1995 and mid-1999, the level of occupation remained relatively stagnated. In its turn, the unemployment rate reached a very high peak between 1998 and 1999, resulting from adverse external shocks (Asian and Russian crises).

As of the second half of 1999, there was a substantial increase in the level of occupation. The 2000-2003 period was characterized by the recovery in generation of employment. Such recovery affected the unemployment rate, which

dropped to a lower level after 2001,

however, still with a high average unemployment rate³.

The third period (2004-2008), in its turn, managed to maintain the process of generating employment, as well as a consistent drop in the unemployment rate.

What are the elements that could

explain this evolution of the unemployment rate and the level of occupation? An obvious bet may be the economic growth rate. The increase in the level of activity tends to be associated with the higher demand for productive inputs from companies, thus justifying a higher level of employment. In fact, the particularly favorable dynamism of the Brazilian labor market after 2004 was positively affected by the economic growth momentum during the period, when the GDP average real growth rate was 4.8% p.a. (taking into consideration the estimate of 5.4% for 2008).

Nonetheless, economic growth does

Continuous economic growth brought about improvements in the labor market between 2004 and 2008

not seem to be the only relevant factor to

explain the course of employment during the period. The pattern of generation of employment is clearly different when the 1995-1999 and 2000-2003 periods are compared, even though the economic growth rates are quite similar (average real growth of 2% and 2.4%, respectively).

What could be a good explanation for the behavior of employment during the post-99 period? During the 90s, the economy was impacted by two processes that brought about a phenomenon of rationalizing employment (that is, growth with low output-employment elasticity). On one hand, the opening of the economy that began early in the decade exposed

2 Graph 1 combines the PME old series (up to 2002) and the new group (after 2002). Although the change in methodology rendered unfeasible any strict comparison between the amounts found, the graph aims at illustrating the occupation and the unemployment rate trends during the period of reference.

3 The coexistence of a stable and yet high threshold for the unemployment rate vis-à-vis the process of increasing levels of occupation may be explained by an increase in the rate of participation in the labor market during this period.

the economy to more foreign competition, spurring on firms' need for gains in productivity. On the other, the overvalued exchange rate regime dominant during the second half of this decade meant more exposure of the economy to this foreign competitive pressure.

The exhaustion of firms adapting to the opening of the economy at the turn of 2000 was capital in explaining the employment recovery during the period. After the reorganization and streamlining of these companies to the reality of the new competition, room was made for economic growth to be accompanied, once again, by an expansion in employment. On the other hand, while adapting to the "shock", the restructuring process of firms involved "downsizing" manpower.

The change to the macroeconomic system in 1999 was also relevant for the recovery in employment. In fact, the depreciation of the Brazilian Real that followed the change in the exchange rate regime meant more protection for the economy, specifically for industry.

With this, economic growth is an important factor in explaining the good performance of the Brazilian labor market, especially the acceleration of the employment generation process and the drop in the unemployment rate

after 2004. However, it is important to bear in mind that the exhaustion of companies' technological and organizational restructuring process, as well as the adoption of a floating exchange rate regime, represents relevant structural factors to understand the disruption of the pattern in employment generation after 1999.

Evidence of crisis in the Brazilian labor market

The current international financial crisis has adversely impacted employment in several countries, and

Brazil has just started to feel its effects. The impact of the crisis on

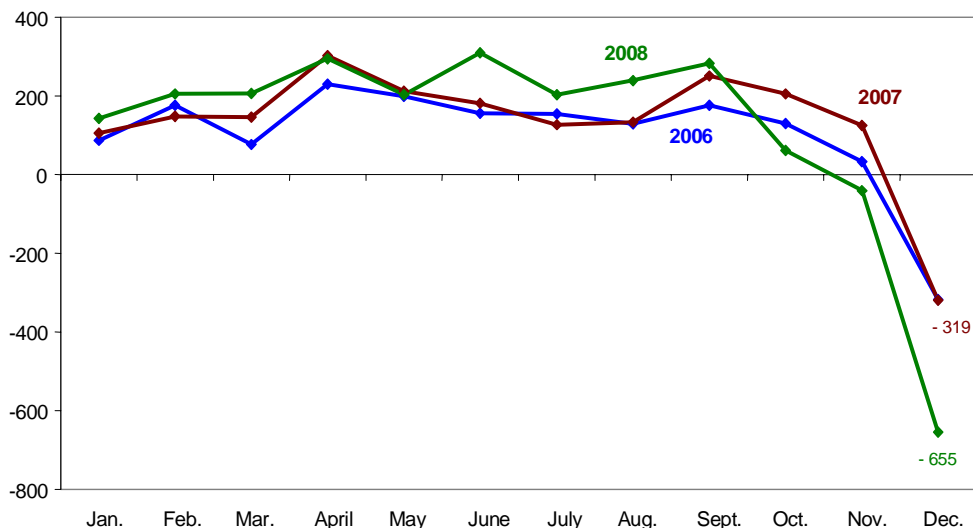
the Brazilian labor market may be substantiated by data from the General Record of Employed and Unemployed People of the Ministry of Labor and Employment (*Cadastro Geral de Empregados e Desempregados/Ministério do Trabalho e Emprego - CAGED/MTE*). This dataset, in spite of covering solely registered employment in the economy, has a higher nationwide representativeness (as seen beforehand, data from PME cover only large urban centers).

Graph 2, which addresses the net employment balance over the last three years shows that the impact of the crisis on the Brazilian labor market, in

In Brazil, the impact of the financial crisis on employment was first perceived in the fourth quarter of 2008

Graph 2

**Net Employment Balance: Recent Years
(thousand)**



Source: CAGED/MTE

terms of generating employment, took actual effect in 4Q2008.

The net creation of work in 2008 surpassed the figures of the two preceding years up to September. In October and November, the net balance lost momentum and, in December, there was a surprisingly high net number of positions eliminated. During this last month, this number reached 655,000 jobs, double that posted in the two preceding years.

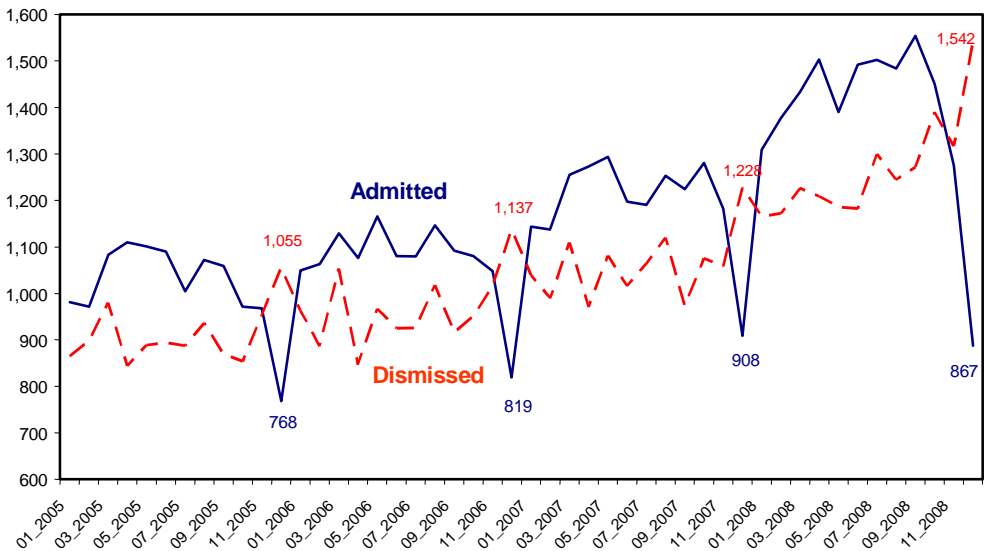
An interesting point to be emphasized is that the high net number of eliminated jobs in December 2008 may be better explained by a lack of hirings than by an actual increase in

dismissals. Graph 3 shows the evolution of admissions and dismissals in the labor market since 2005. As can be seen, December is the month that often records a negative net balance for seasonal reasons, with a drop in admissions and an increase in dismissals vis-à-vis the other months of the year. In 2008, however, while the increase in dismissals between November and December was a slightly higher than the trend observed in the preceding years, the drop in hirings was prominent and unparalleled.

Thus, the negative outcome of December, although substantially higher than that recorded in previous

Graph 3

Admitted and Dismissed People (thousand): 2005-2008



Source: CAGED/MTE

years, seems to have an underlying pause in production and investment decisions in view of growing economic uncertainties, rather than implying a reversal in the pattern of employment generation.

Perspectives for unemployment in Brazil

The acceleration in economic growth in Brazil as of 2004 was an important factor to explain the drop in the Brazilian unemployment rate. The expectations, however, are that GDP growth will slow down in the next few years within a scenario of international financial crisis.

In the late 90s, there was a marked

increase in the Brazilian unemployment rate, in a scenario of slowing economic growth, also trailing behind international crises. An interesting point is to discuss whether this estimated reduction of the Brazilian economic growth could cause the unemployment rate to rise dramatically over the next few years.

As already pointed out, although economic growth is important, other factors significantly helped shed light on the recovery of the employment level in the Brazilian economy. And, moreover, most of these factors do not tend to be affected by the crisis, or involve mechanisms to lessen the impact of the crisis on employment.

The “shock” brought on by the opening of the economy in the early 90s has already been absorbed by companies. Also, during the current crisis, a new opening of an economy of that size is not likely to take place. On the other hand, the floating exchange rate ensures a protection mechanism with regards to foreign competition, especially at times when the crisis worsens: any harm to the balance of payments tends to be followed by a fall in the exchange rate, boosting exports and discouraging imports.

Besides this, qualitative changes that occurred in the Brazilian labor market tend to offer better employment protection.

There was a qualification enhancement and a consequent

increase in the productivity of the employed workforce – the participation of workers with lower qualification (lower than Elementary School) in registered employment dropped from 33.5% in 2000 to less than 20% in 2007.

There was also a recovery in registered employment – owing mostly to the recovery of industry in the economy. Between 2001 and 2007, the percentage of registered employment increased around 5 points, reaching approximately 45% of citizens with an occupation (Ramos et alli, Boletim Mercado de Trabalho Nº. 37, IPEA – data from the PNAD).

The elimination of one registered position poses a number of corporate costs, and the dismissal of more productive workers involves a higher cost in opportunity for the employer. These recent changes in the employment market are expected to bring about higher resistance to the elimination of jobs.

With this, a certain increase in the Brazilian unemployment rate may be already forecast in a scenario characterized by a process of economic slowdown. However, it is important to note that the macroeconomic policy and the conditions of the economic structure are quite different from those prevailing in the second half of the 90s.

Thus, the crux of the issue is that the Brazilian economy is currently furnished with companies adapted to an environment of higher competitiveness, an exchange rate regime that is more favorable to moderate foreign shocks, as well as qualitative changes in the labor market, such as the increase in registered positions and in worker qualification. These changes, that have taken place since the late 90s, point toward a preservation of positive dynamics within the Brazilian employment market. Hence, in this scenario, lower growth rates are not expected to be translated into a dramatic reversal of the gains achieved over the last few years.

The increase in registered work and qualification of employees may lower the impact of the crisis on the labor market





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